

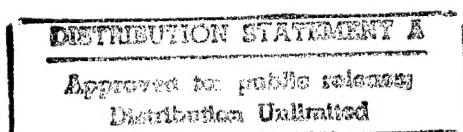
Statement of
The Under Secretary of Defense for Acquisition and Technology
Honorable Paul G. Kaminski

Before the
Subcommittee on Seapower
of the
Senate Committee on Armed Services
on
C-17 Multi-Year Procurement Request

March 28, 1996

Mr. Chairman, members of the subcommittee, thank you for the opportunity to appear today to discuss our proposed multi-year procurement plans for one of the Department's most important priorities—the C-17 Globemaster III airlifter. With your strong support and direction, we have worked diligently to make strategic mobility improvements. The C-17 is helping us make tangible gains in mobility right now. This aircraft is indeed earning its reputation as the world's most versatile and capable airlifter.

As you know, in early November 1995, I chaired a Defense Acquisition Board (DAB) review of the C-17 program and the Non-Developmental Airlift Aircraft (NDAA) alternative. This DAB was the culmination of the two-year probationary period that my predecessor instituted. In the past two years, McDonnell Douglas and the Air Force undertook a massive effort at restructuring and reorganizing the program, with the aim of reducing cost, improving performance, and increasing quality. The result? We saw the unit price of C-17s come down substantially, no doubt spurred on by the competition with the NDAA. We saw quality markedly improve. We saw early deliveries of aircraft to the operational user start and continue unabated to date.



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But that was not enough. To gauge the progress of these efforts against stated requirements, several extraordinarily detailed analyses were presented to the DAB. The Cost and Operational Effectiveness Analysis (COEA), known as the Strategic Airlift Force Mix Analysis, perhaps the most detailed strategic airlift analysis in history, showed that there was no question that a substantial number of C-17s beyond 40 were required. Another, called the Tactical Utility Analysis, examined the utility of the C-17 in scenarios other than strategic airlift in Major Regional Contingencies (MRCs), such as intra-theater airlift, airdrop, and lesser regional contingencies. It showed that the C-17 brought operational commanders and the nation important new capabilities and increased flexibility in the changing world situation.

When we carefully analyzed the effect of small changes to the analytical assumptions, it confirmed that the C-17 was the most robust alternative in responding to the expected range of operational conditions. Finally, the C-17's affordable life cycle price, which was less than one percent higher than the equivalent mixed fleet, made it clear that an additional 80 C-17s was the right choice for the Department and the taxpayer. In what way? Allow me to illustrate.

For example, during Operation Joint Endeavor, when it became clear that due to weather, diplomatic constraints, and sheer volume (the railways and roadways were backed up) C-17s were used to haul outsized cargo, like howitzers and Bradley Fighting Vehicles, directly to Tuzla, Bosnia. When we discovered that it was either impossible or impractical to move critically needed, outsized bridging equipment via the roads or rail, we flew it in on the C-17. Let me point out that no one ever envisioned or modeled the ability of the C-17 to carry bridging equipment on flatbed trucks so that it could be driven right to a flooded river. But when the real-world need arose, the C-17 was ready. I attribute this airlifter's extraordinary ability to handle real-world challenges to the inherent flexibility and military utility designed into the C-17. I am certain we will

hear many more accounts—like the missions flown in support of the Sava River bridging operation as users learn new ways of employing this impressive capability.

The statistics compiled during the Operation Joint Endeavor deployment were impressive. C-17s flew a quarter of the airlift missions, yet moved about half of the cargo. These aircraft, operational only for a year, maintained a departure reliability rate of 97 percent in the stress of a real-world operations. Also, the ability to use small austere airfields enabled the C-17 to operate effectively at Tuzla, where the C-5 could not. Although C-130s could operate at such smaller fields, each C-17 into Tuzla could deliver the equivalent of four average C-130 loads—that is getting combat power where you need it, fast. These are just a few of the many examples of how the results of our analyses and the Department's C-17 decision are being borne out in the real world.

You are no doubt aware that the warfighting CINCs identify strategic lift as Department's greatest single deficiency. They unanimously identified the C-17 as having highly preferable capabilities that give them the type of crucial operational flexibility just described. With its ability to operate from small airfields and in hostile environments, to deliver oversize and outsize cargo wherever we need it, the C-17 is an essential resource for our warfighters.

REQUIREMENT

General Shalikashvili firmly supports the C-17 requirement. Quoting from testimony before the House Appropriations Committee on March 7, 1996, he said " . . . we must continue to improve our strategic lift. I think that we are making good progress in improving our airlift and . . . we must pass the multi-year procurement for the C-17." He has told the Secretary of Defense that his number one priority with respect to strategic airlift is the C-17 multi-year procurement because it offers the best opportunity to meet military needs at the most affordable price.

The C-17 program has a stable requirement. The total requirement is 120 C-17s and is based on detailed analyses. This C-17 procurement requirement is expected to remain unchanged in terms of production rate, fiscal year phasing, and total quantity. There are some who would argue against a multi-year procurement (MYP) now — just wait a little longer until requirements are re-examined, they say, and maybe you will not need 120 C-17s. In my judgment, with a well-documented need for lift, additional waiting is not warranted.

Nonetheless, I asked for an analysis of the MYP proposal to assess the impact of requirements changes. The analysis shows that even if we have to break the multi-year buy and stretchout the procurement of the 120 aircraft buy, this multi-year approach still saves money so long as we do not reduce the planned rate until after FY 1998. If we buy fewer than 120, this multi-year approach saves money so long as we do not cancel orders until after FY 2000. In that time we will buy 45 more C-17s for a total of 85 aircraft. We clearly need more than 85 C-17s, so any fear that we are tied into a deal that restricts our maneuver room is unfounded.

The C-17 program has stable funding. It is one of the Department's top, near-term modernization priorities. The budget necessary to execute the proposed program has already been programmed through and beyond the Future Years Defense Program (FYDP) and in the FY 1997 President's Budget. The Department is committed to fund the program at the required level to ensure the contract is completed.

The C-17 configuration is technically mature. The C-17's excellent performance during operations in Bosnia attests to that. The developmental and initial operational test programs are complete, and the aircraft now has fourteen months of operational experience. The configuration was baselined with the eighth production lot, and the proposed multi-year purchase begins with the ninth lot.

MULTI-YEAR REQUEST

Mr. Chairman, allow me to take a moment to review the C-17 program to help you better understand why the Department believes a multi-year procurement is in our interests. As you are acutely aware, not very long ago this program was in big trouble. With your help, we have made great strides in turning this program into one we all can be proud of. Since the comprehensive settlement was approved by the Congress, and thanks to a variety of cost reduction initiatives, we have already cut the unit price nearly in half.

The price of the first 40 C-17 aircraft, in constant FY 1996 dollars, was an average of \$338 million per copy. With the maximum affordable rate change and the proposed multi-year procurement, we will bring the average price down to \$173 million (in constant FY 1996 dollars). Simultaneously, we have seen the quality of delivered aircraft steadily improve. In a nutshell, the aircraft is demonstrating that it is reliable, extraordinarily capable, and cost-effective.

We are now requesting legislative approval for the C-17 multi-year procurement. I believe the program meets the criteria for such a procurement, and it constitutes what I think is a sound business decision. Multi-year contracting is important to the Department because it leverages our available procurement funds. We get more rubber on the ramp for the same investment when we use multi-year contracting.

Savings and Cost Avoidance

The proposed multi-year contract will save the government approximately \$896 million over the best prices available by contracting in annual increments for the same 80 aircraft at the same production rate. Next to the B-1 program, this will be the largest

multi-year related cost avoidance in the Department's history. This provides funds that will be used to bolster other critical modernization efforts. It is also important to remember that the additional five percent savings comes on top of the substantial cost reductions achieved in our long-term, fixed price buyout strategy already in place, which reduced prices 27 percent. The last seven percent of this reduction was associated with maximum affordable rate efficiencies. Additionally, the five percent reduction figure is based upon actual, negotiated contracts, and not upon estimates or proposals, so I am confident these are real savings. When taken in context of the C-17's previous price reductions, in particular the seven percent reduction for rate efficiencies, the further five percent reduction is a good deal for the Department and the nation.

Impact on Industrial Base

A multi-year contract will foster a stable environment in which the C-17 industrial base can grow stronger. As a result, we believe the major and critical subcontractors will be able to build components at, or near, commercial prices. Through multi-year contracting, it becomes affordable to qualify dual sources for critical lower-tier suppliers, increasing competition and reducing risk. Of course, the long-term commitment permits better planning for capital investments, and more efficient production of economic lot quantities. This alone is likely to help the many small suppliers, by allowing them to make cost-effective decisions on a longer-term basis.

IMPLEMENTATION

To arrive at this multi-year proposal, we conducted an extensive and cooperative "Should Cost" review. We developed a joint contractor-government cost and pricing model that was based on actual data for the 25 aircraft produced to date. We also

negotiated a fixed price contract with fixed price options (containing adjustment clauses) for 120 C-17s.

In preparing this proposal for delivery to the Congress, we should have better laid the basis for the June 1996 approval need date first. We presented and discussed legislative options with all four Defense oversight committees, and found that there were limited legislative vehicles that would meet the June 1996 date. It is clear to us that there is a window of opportunity that behooves us to act by June 1996, rather than later in the fall when the FY 1997 budget cycle is expected to be completed. The majority of savings will be captured when McDonnell Douglas can negotiate with its suppliers on a long-term basis. For example, to meet the FY 1997 aircraft delivery schedule for Lot 9, or aircraft 41-48, McDonnell Douglas must negotiate and activate 50 percent of its subcontracts with first-tier suppliers and vendors by June 1, 1996. Since more than 60 percent of the C-17 is built by suppliers and vendors, a significant portion of the multi-year savings are tied to economic order quantity (EOQ) efficiencies realized by first-, second-, third-, and in many cases, fourth-tier suppliers.

For a significant delay beyond June 1996, EOQ-funded producibility enhancements will benefit fewer C-17s. Without multi-year approval, McDonnell Douglas will be forced to negotiate contracts for the eight aircraft in Lot 9 during the summer of 1996. With multi-year contracting approval, McDonnell Douglas could negotiate prices for 80 aircraft. There is a substantial amount of savings, on the order of \$500 million, in that ten-fold increase in production quantity. If we miss Lot 9, ten percent of the remaining C-17 production run will not benefit from EOQ efficiencies.

If we wait until the FY 1997 budget cycle is complete, we could delay EOQ purchases and producibility enhancements to Lot 10 or beyond. In this case, 21 percent of the remaining C-17 production would not benefit from EOQ purchases. We would also erode the confidence of vendors and suppliers that a multi-year procurement

would ever come to pass. This would cause vendors to be more conservative and would lead to protracted contracted negotiations and further delays in realizing EOQ savings.

SUMMARY

In conclusion, I welcome this opportunity to appear before the subcommittee today. The Department is requesting legislative approval for: (1) a multi-year procurement contract; (2) a waiver of section 2306b(1), 10 USC to extend the multi-year procurement duration from five to seven years; and (3) use of prior-year funds for the Economic Order Quantity (EOQ) purchase in FY 1996. We are seeking approval ahead of the FY 1997 budget cycle (June 1, 1996 requested) in order to execute the MYP proposal.

I sincerely believe this is a good news story – one that leverages more than a billion dollars in procurement funding. The C-17 MYP offer on the table is a good one. I believe that the C-17, thanks to the efforts of the Congress, the Department of Defense, the Air Force, and McDonnell Douglas, is proving itself to be worth the commitment.